

Message Text

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SUBJECT: THE MALAYSIAN TIN INDUSTRY

REFS: A) 77 LA PAZ 10155 (NOTAL), B) KUALA LUMPUR 0071 (NOTAL)

1. SUMMARY: MANY OBSERVERS HAVE ARGUED THAT THE DECLINE IN MALAYSIAN TIN PRODUCTION, WHICH DROPPED 25 PERCENT BETWEEN 1972 AND 1976, WAS LARGELY DUE TO A SERIES OF POLICY MEASURES ADOPTED BY THE GOM. THESE INCLUDED HIGH RATES OF TAXATION, MEASURES DESIGNED TO GIVE MALAYSIAN (ESPECIALLY MALAYS) A LARGER SHARE OF THE TIN INDUSTRY AND INCREASINGLY RESTRICTIVE LAND POLICIES BY THE STATES (WHICH, UNDER MALAYSIAN CONSTITUTION, CONTROL LAND MATTERS). WE HAVE RECENTLY RE-EXAMINED THE MALAYSIAN TIN SITUATION. OUR FIRST CONCLUSION IS THAT WHILE GOM ACTIONS HAVE HAD AN IMPACT, THE PRIMARY REASON FOR DECLINE IN MALYSAIN TIN PRODUCTION IS EXHAUSTION OF EASILY RECOVERED TIN RESERVES.

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RECENT ORE DISCOVERIES, BETTER TECHNOLOGY AND HIGHER PRICES HAVE ALL COMBINED TO INCREASE DRAMATICALLY ESTIMATES OF MALAYSIA'S RECOVERABLE RESERVES. FURTHERMORE, GOM HAS TAKEN STEPS INDICATING THAT IT TOO IS CONCERNED WITH HEALTH OF TIN INDUSTRY. TWO MOST IMPORTANT DEVELOPMENTS ARE DIRECTLY RELATED. FIRST, GOM, ACTING THROUGH A PUBLIC CORPORATION, HAS PURCHASED LOND TIN, WHICH IS INVOLVED IN MAJOR SHARE OF DREDGING SECTOR. SECOND, IT IS USING THIS

CORPORATION TO ENTER INTO JOINT VENTURES WITH THE STATES ON TERMS THAT WILL GIVE STATES MAJOR RETURNS FROM TIN, THUS DIRECTLY INVOLVING THEM IN INDUSTRY'S FUTURE WELL-BEING. OTHER IMPORTANT DEVELOPMENTS INCLUDE USE OF FISCAL POLICY TO PROVIDE STATE GOVERNMENTS WITH GREATER REVENUES FROM TIN SO THAT THEY WILL HAVE INCENTIVE TO BE MORE COOPERATIVE WITH MINING COMPANIES AND LIFTING FROM INDUSTRY REQUIREMENT TO FINANCE MALAYSIA'S BUFFER STOCK CONTRIBUTIONS.

ALL OF THIS HAS LED US TO A MORE OPTIMISTIC VIEW OF MALAYSIA'S PRODUCTION PROSPECTS OVER TIME. WE HAVE FURTHERMORE CONCLUDED THAT THE LONG-TERM EQUILIBRIUM PRICE FOR TIN MAY WELL BE HIGHER THAN ITS PRESENT PRICE AND THAT THE MALAYSIAN TIN INDUSTRY IS REPLYING TO MARKET SIGNALS IN TERMS OF NEW INVESTMENT BUT THAT CONSIDERABLE TIME WILL BE REQUIRED BEFORE NEW PRODUCTION COMES ON LINE. END SUMMARY.

2. BACKGROUND. IN 1972, MALAYSIA PRODUCED 76,830 METRIC TONS OF TIN, AN ALL-TIME HIGH. OF THAT AMOUNT, 55.7 PERCENT WAS PRODUCED BY THE 940 GRAVEL PUMP OPERATIONS THEN IN EXISTENCE. IN 1976 MALAYSIAN TIN PRODUCTION HAD DROPPED TO 63,401 METRIC TONS OF WHICH 49.9 PERCENT WAS PRODUCED BY 724 GRAVEL PUMP OPERATIONS. IN OTHER WORDS, WITHIN FOUR YEARS, MALAYSIAN TIN PRODUCTION DECLINED BY 25 PERCENT WHILE THE NUMBER OF GRAVEL PUMP MINES IN OPERATION DECLINED BY 23 PERCENT.

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3. NEW ECONOMIC POLICY.

A) FOLLOWING THE RACIAL RIOTS OF 1969, THE GOM DECIDED TO UNDERTAKE A POLICY THAT WOULD ENSURE THAT THE ECONOMICALLY BACKWARD MALAYS OBTAINED A MORE SIGNIFICANT POSITION IN THE COMMERCIAL LIFE OF THE COUNTRY. THIS WAS REFLECTED IN THE TIN INDUSTRY IN TWO WAYS--PRESSURE ON THE FOREIGN COMPANIES IN THE DREDGING SECTOR TO REDUCE THEIR SHARE OF EQUITY AND ON THE CHINESE GRAVEL PUMP OPERATORS THROUGH MANIPULATION OF LAND POLICIES BY THE STATES. THE PRESSURE ON THE FOREIGN COMPANIES WAS IMPOSED THROUGH MORAL SUASION, BUREAUCRATIC HARASSMENT AND THREATS OF WITHHOLDING LEASE RENEWALS. THE RESULT WAS THAT FOREIGN COMPANIES DROPPED NEW INVESTMENT PLANS AND TRIED TO MAXIMIZE PROFITS IN THE SHORT RUN.

B) IN THE MOST SIGNIFICANT DEVELOPMENTS TO DATE, THIS SITUATION HAS DRAMATICALLY IMPROVED. FIRST, ACTING THROUGH PERNAS, A PUBLIC SECTOR CORPORATION, THE GOM HAS OBTAINED AN IMPORTANT OWNERSHIP ROLE IN THE DREDGING SECTOR. THIS WAS ACCOMPLISHED THROUGH OPEN MARKET PURCHASE OF THE STOCK OF LONDON TIN ON THE LONDON STOCK EXCHANGE. AS A RESULT, A NEW ENTITY KNOWN AS THE MALAYSIAN MINING CORPORATION (MMC--OF WHICH PERNAAS OWNS 71.35 PERCENT OF THE EQUITY) HAS BEEN FORMED WHICH OWNS EQUITY IN THE

OPERATIONS OF 80 PERCENT OF THE DREDGES IN MALAYSIA. THIS HAS MEANT THE END OF THE LONG AND FREQUENTLY BITTER STRUGGLE BETWEEN MAJOR BRITISH MINING INTERESTS AND THE GOM. THE SECOND IMPORANT DEVELOPMENT IS THAT MMC, WHICH IS SERIOUSLY INTERESTED IN EXPANSION, IS ACTIVELY NEGOTIATING JOINT VENTURES WITH THE STATES ON TERMS SO FAVORABLE TO STATE INTERESTS THAT THEIR COOPERATION IN EXPANDING PRODUCTION IS VIRTUALLY ASSURED. MMC IS ON THE VERGE OF ANNOUNCING FORMAL AGREEMENT ON A JOINT VENTURE WITH THE STATE OF SELANGOR WHEREBY THE STATE WILL HAVE 70 PERCENT OF THE OWNERSHIP AND MMC 30 PERCENT. FURTHERMORE, MMC IS ACTIVELY NEGOTIATING WITH TWO OTHER STATES FOR PNM TULE JOINT VENTURES ALONG THE SAME LINES. IF THESE MATERIALIZE, THEY COULD LEAD TO FIVE NEW DREDGES BEING IN OPERATION BY THE EARLY 1980'S ON LAND NOT NOW BEING MINED.

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4. RESERVES.

A) INTENSIVE TIN MINING HAS SUBSTANTIALLY DEPLETED MANY OF THE EASILY ACCESSIBLE TIN RESERVES IN MALAYSIA. OVER THE LONG TERM, THE MALAYSIAN TIN INDUSTRY WILL HAVE TO SEARCH MUCH HARDER FOR TIN RESERVES AND THESE WILL BE MUCH MORE EXPENSIVE TO EXTRACT. THE EXTENT OF MALAYSIA'S TIN RESERVES HAS ONLY BEEN INVESTIGATED IN A RELATIVELY SUPERFICIAL FASHION. THE LAST FORMAL ESTIMATE (WHICH WAS PREPARED BY TIN INTERNATIONAL IN 1973) LISTED

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MALAYSIA'S MEASURED AND INDICATED RESERVED AT 600,000 LONG TONS AND INFERRED (POSSIBLE) RESERVES OF 230,600 FOR A TOTAL OF 830,600 LONG TONS OF METAL. THE SAME REPORT ESTIMATED INDONESIA'S RESERVES AT 2.4 MILLION LONG TONS AND THAILAND'S AT 1.2 MILLION LONG TONS. PUBLIC AND PRIVATE SECTORS HAVE CLEARLY INDICATED THAT THESE RESERVE ESTIMATES ARE SURELY TOO LOW. THE REAL QUESTION TO BE ANSWERED WITH REGARD TO MALAYSIAN TIN SEEMS TO BE AT WHAT PRICE LEVEL WILL PRODUCERS BE WILLING TO EXTRACT IT. B) A DREDGE HAS RECENTLY GONE INTO OPERATION NEAR KUALA LUMPUR (AT AYER HITAM) ON SUBSTANTIAL DEPOSITS THAT WERE TOO DEEP (230 FEET) FOR DREDGING WITH THE TECHNOLOGY OF TEN YEARS AGO AND OF A QUALITY THAT WAS NOT THOUGHT ECONOMIC AT PREVIOUS TIN PRICES. IN ANOTHER MOVE OF MAJOR SIGNIFICANCE, THE MALAYSIAN MINING CORPORATION (THE GOM-CHARTER CONSOLIDATED JOINT VENTURE, FORMERLY KNOWN AS NEW TRADEWINDS, WHICH HAS AN IMPORTANT SHARE IN MANY OF THE DREDGING COMPANIES IN MALAYSIA) WILL SOON ANNOUNCE AGREEMENT WITH THE SELANGOR STATE GOVERNMENT TO PROCEED WITH LIMITED OFFICIAL USE

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PLANS FOR OPERATIONS AT KUALA LANGGAT ON LAND SIMILAR TO BUT EVEN DEEPER THAN THAT AT AYER HITAM. ESTIMATES OF PROVEN RESERVES INDICATE THIS FIELD COULD YIELD AT LEAST 375,000 LONG TONS OF METAL (SOME ESTIMATES DOUBLE THIS FIGURE) OVER 2 25 YEAR PERIOD (AT 15,000 TONS PER ANNUM). REPORTS INDICATE THAT THIS MAY BE THE LARGEST FIND OF TIN EVER RECORDED AND EVEN LARGER THAN THE KINTA VALLEY. THESE RESERVES WERE NOT INCLUDED IN THE 1973 ESTIMATES AND HAVE THE EFFECT OF INCREASING THEM IN ONE SWOOP BY 63 PERCENT.

C) THIS FIELD, LIKE MUCH OF THE ENTIRE WEST COASTAL PLAIN OF PENINSULAR MALAYSIA, HAS A RELATIVELY THICK OVERBURDEN (300 AND MORE FEET) AND THERE IS CONSIDERABLE EXPECTATION THAT EVEN MORE SUBSTANTIAL TIN RESERVES EXIST UNDER IT. LITTLE EXPLORATION FOR TIN HAS TAKEN PLACE IN THIS AREA PREVIOUSLY BECAUSE THE TECHNOLOGY IN THE PAST WAS NOT WELL ENOUGH DEVELOPED TO GO DEEP ENOUGH TO EXTRACT THE ORE, THE TIN PRICES WERE NOT HIGH ENOUGH TO WARRANT ITS EXTRACTION, AND EXTENSIVE MINING WOULD INTERFERE WITH EXISTING LAND USES, SUCH AS RUBBER AND OIL PALM PLANTATIONS. IN ADDITION, MUCH OF THE REST OF PENINSULAR MALAYSIA REMAINS UNEXPLORED GEOLOGICALLY AND THERE IS SOME HOPE THAT AS MORE

INTENSIVE GEOLOGICAL SURVEYS ARE CONDUCTED MORE TIN WILL BE LOCATED. THERE IS ALSO SOME EVIDENCE THAT MALAYSIA HAS OFFSHORE

TIN DEPOSITS BUT THESE ARE NOT AT PRESENT ECONOMICALLY FEASIBLE TO MINE. PRIVATE PROSPECTING HAS DECLINED IN RECENT YEARS BECAUSE OF STATE POLICIES WHEREBY A PROSPECTOR OFTEN DOES NOT RECEIVE A LEASE ON TIN-BEARING PROPERTY HE HAS DISCOVERED. FINALLY, ENVIRONMENTAL PRESSURES ARE CERTAIN TO INCREASE ON THE INDUSTRY, THUS ADDING TO COSTS OVER TIME.

5. TAXATION.

A) THE TIN INDUSTRY IS AMONG THE MOST HEAVILY TAXED IN MALAYSIA. A RECENT INDUSTRY SURVEY ESTIMATED TAXES ON TIN MINERS AT LIMITED OFFICIAL USE

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35.1 PERCENT OF GROSS INCOME AT A SALES PRICE OF M\$1250 PER PIKUL. THE INDUSTRY THUS FACES THE FOLLOWING TAXES: IMPORT DUTIES WHICH EFFECT A WIDE RANGE OF EQUIPMENT; EXPORT DUTY (INTO WHICH THE GOM HAS JUST MERGED ITS EXPORT SURCHARGE) WHICH ACCOUNTS FOR 72 PERCENT OF GOM REVENUES OBTAINED DIRECTLY FROM TIN; INCOME TAXES (25 PERCENT OF GOM TIN REVENUES) AND THE TIN PROFITS TAX WHICH ACCOUNTS FOR THREE PERCENT OF TIN REVENUES. IN ADDITION, MALAYSIA HAS AN EXCESS PROFITS TAX WHICH OCCASIONALLY HITS THE INDUSTRY, ESPECIALLY THE DREDGE OPERATORS, HARD.

B). ONE OF THE BY-PRODUCTS OF THESE HIGH LEVELS OF TAXATION IS THE DEGREE OF SMUGGLING OF TIN TO SINGAPORE THAT TAKES PLACE. INDUSTRY SOURCES ESTIMATE THAT 7 PERCENT OF MALAYSIA'S TOTAL PRODUCTION (OR ABOUT 4,400 LONG TONS IN 1976) IS SMUGGLED OUT. SINGAPORE, WHICH HAS NO TIN PRODUCTION, HAD NET EXPORTS OF OVER 4,000 TONS OF TIN IN 1976. IT IS ALSO NOTABLE THAT THE MAJOR DECLINE IN MALAYSIA'S TIN PRODUCTION BEGAN IN 1974 WHEN A DROP OF OVER 4,000 TONS WAS REGISTERED. 1974 WAS THE YEAR THAT MALAYSIA IMPOSED THE EXPORT SURCHARGE AND IS PROBABLY WHEN HEAVY SMUGGLING TO SINGAPORE BEGAN. MANY INDUSTRY SOURCES STATE THAT THE REASON FOR THE SMUGGLING IS THE HIGH RATE OF EXPORT TAX AND SURCHARGE TOGETHER (WHICH ACCOUNT FOR ROUGHLY 25 PERCENT OF THE TOTAL COST OF TIN).

C) THE GOM HAS RECENTLY TAKEN TWO STEPS THAT ARE DESIGNED TO EASE THE DIFFICULTIES THE INDUSTRY FACES. IT HAS MERGED THE TIN SURCHARGE WITH THE TIN EXPORT DUTY. THE STATES SHARE (TEN PERCENT) IN THE EXPORT DUTY BUT NOT IN THE SURCHARGE, WHICH ACCOUNTS FOR 26 PERCENT OF TAX REVENUES GENERATED. WITH THIS CHANGE, THE STATES WILL NOW RECEIVE 10 PERCENT OF THE MERGED EXPORT DUTY AND SURCHARGE, THUS INCREASING THE BENEFIT THEY DERIVE. THIS SHOULD PROVIDE GREATER INCENTIVE TO COOPERATE WITH THE TIN INDUSTRY. SECONDLY, THE GOM HAS NOW AGREED TO PAY THE COST OF THE MALAYSIAN CONTRIBUTION TO THE TIN STOCKPILE. MOST RECENTLY, THIS AMOUNTED TO ABOUT 3.8 PERCENT OF THE SALE PRICE OF EACH PIKUL OF TIN. WE BELIEVE THESE MOVES HAVE MORE LIMITED OFFICIAL USE

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BENEFIT FOR THE TIN INDUSTRY THAN OUR ORIGINAL ASSESSMENT.

6. LAND ISSUES.

UNDER THE MALAYSIAN FEDERAL CONSTITUTION, LAND MATTERS ARE RESERVED FOR THE STATES, WHICH JEALOUSLY GUARD THEIR PEROGATIVES IN THIS AREA. AS A RESULT OF STATE POLICIES FAVORING MALAYS OVER CHINESE AND FOREIGN INTERESTS AND THE GENERAL INEFFICIENCY OF THE STATE BUREAUCRACIES, GRAVEL PUMP COMPANIES (WHICH ARE MOSTLY CHINESE) HAVE HAD SUBSTANTIAL DIFFICULTIES IN THE PAST IN EITHER OBTAINING NEW LEASES OR IN RENEWING OLD ONES. THIS HAS DISCOURAGED EXPANSION INTO NEW OPERATIONS. A SEPARATE PROBLEM IS COMPETING USES OF LAND THAT MAY HAVE TIN RESERVES UNDER IT. INDUSTRY SOURCES BELIEVE THAT THERE IS A CONSIDERABLE AMOUNT OF TIN BEARING LAND (IN ADDITION TO THE DEEP DEPOSITS MENTIONED ABOVE) THAT IS PRESENTLY BEING USED IN AGRICULTURE OR IS IN FOREST RESERVE LANDS. THE PRICE DEMANDED FOR THESE

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LANDS IS SO HIGH AS TO MAKE THEIR USE FOR MINING
UNECONOMIC AT PRESENT PRICE LEVELS.

7. COMMENT. BASED ON THIS SURVEY, WE BELIEVE THAT THE DIFFICULTIES WHICH HAVE PLAGUED MALAYSIA'S TIN INDUSTRY FOR YEARS ARE MODERATING AND THAT IT IS POSSIBLE TO LOOK DOWN THE ROAD WITH SOME OPTIMISM. THIS IS NOT TO ARGUE THAT THE INDUSTRY WILL REMAIN THE SAME OR THAT PRODUCTION WILL INCREASE IN THE NEXT FEW YEARS. NEITHER OF THESE IS LIKELY TO HAPPEN. IN PARTICULAR, THE ROLE OF GRAVEL PUMP OPERATIONS HAS CHANGED AND WILL CHANGE MORE DRAMATICALLY IN THE FUTURE. THE PRINCIPAL REASON THAT THE NUMBER OF GRAVEL PUMP OPERATORS HAS DECLINED IS THAT THE KINDS OF DEPOSITS BEST SUITED FOR THEIR OPERATIONS ARE FAST DISAPPEARING. AS THE DEPOSITS GET SMALLER AND DECLINE IN QUALITY, THE TREND HAS BEEN FOR THE MERGER OF SEVERAL SMALLER COMPANIES INTO LARGER UNITS TO MINE A WHOLE FIELD. THIS WILL CONTINUE AND THE NUMBER LIMITED OFFICIAL USE

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OF INDEPENDENT GRAVEL PUMP OPERATIONS WILL DECLINE. THE FUTURE IN THE INDUSTRY WILL INCREASINGLY BELONG TO OTHER TYPES OF OPERATIONS: LARGER AND MORE PRODUCTIVE DREDGES ABLE TO GO DEEPER THAN IN THE PAST; MORE OPEN CAST OPERATIONS, AND POSSIBLY SOME OFF-SHORE AND UNDERGROUND MINING. ALL OF THIS MEANS SUBSTANTIALLY HIGHER CAPITAL EXPENDITURES (A NEW DREDGE NOW COSTS ABOUT US\$12 MILLION TO GET INTO OPERATION). IT ALSO MEANS THAT THESE PROJECTS WILL TAKE MUCH LONGER TO GET OFF THE GROUND. FOR EXAMPLE, THE FIVE NEW DREDGES THAT MCC IS CONSIDERING PUTTING INTO OPERATION WILL TAKE FROM THREE TO FIVE YEARS TO BECOME FULLY OPERATIONAL. A FINAL, AND IN SOME WAYS MOST IMPORTANT, DEVELOPMENT HAS BEEN THE ACHIEVEMENT OF PUBLIC/PRIVATE SECTOR HARMONY IN THE DREDGING SECTOR. THIS HAS BEEN ONE OF THE MOST SEVERE CONSTRAINTS ON AN EXPANSION OF THE INDUSTRY AND ITS REMOVAL WILL GREATLY EASE ANY FUTURE PROGRESS.

8. ONE APPARENT CHARACTERISTIC OF MALAYSIAN TIN INDUSTRY HAS BEEN THAT SUPPLY IS COMPLETELY INELASTIC, I.E., REGARDLESS OF PRICE LEVELS, PRODUCTION GOES DOWN. WE NOW BELIEVE THAT THIS MAY BE ONLY TRUE IN THE MEDIUM TERM. EXPANSION PLANS ARE UNDERWAY IN THE INDUSTRY THAT WILL DO MUCH TO STABILIZE MALAYSIAN TIN PRODUCTION IN THE FUTURE. IT WILL BE SEVERAL YEARS, HOWEVER, BEFORE THESE OPERATIONS COME ON LINE AND IT IS ENTIRELY POSSIBLE THAT TIN PRODUCTION WILL CONTINUE TO DECLINE DURING THAT TIME. GIVEN THE HIGH INVESTMENT COSTS FOR NEW DREDGES, OTHER CAPITAL INTENSIVE FORMS OF MINING REQUIRED (ESPECIALLY IN BOLIVIA), AND THE HIGH COST OF SUBSTITUTES, IT WOULD APPEAR

THE LONG TERM EQUILIBRIUM PRICE FOR TIN MAY WELL BE HIGHER THAN ITS PRESENT PRICE.

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9. WHILE THE ABOVE FACTORS PROMISE TO STIMULATE MALAYSIAN TIN PRODUCTION, WE BELIEVE IT MAY BE POSSIBLE TO HASTEN THE PROCESS BY SEEKING CERTAIN ACTIONS ON THE PART OF THE GOM. FIRST, MALAYSIA IS IN GREAT NEED OF AN INTERGRATED MINERALS POLICY, ESPECIALLY WITH RESPECT TO TAXATION, LAND AND INVESTMENT. THE GOM IS GROING ITS WAY TOWARDS SUCH A POLICY (THE MINISTRY OF PRIMARY INDUSTRIES IS WELL AWARE OF THE NEED FOR ONE AND IS WORKING ON IT) BUT BUREAUCRATIC RESISTANCE AND FOOT-DRAGGING IN OTHER MINISTRIES STILL HINDER ITS FORMULATION AND IMPLEMENTATION. IF THE CONSUMERS PUSH FOR ITS DEVELOPMENT, IT IS MUCH MORE LIKELY TO RECEIVE HIGH LEVEL ATTENTION AND SUPPORT. SECONDLY, WE SHOULD URGE THE GOM TO REDUCE FURTHER ITS TAXES ON TIN PRODUCTION. FINALLY, WE MIGHT CONSIDER OFFERING MALAYSIA THE SERVICES OF THE U.S. GEOLOGICAL SURVEY, EVEN ON A REIMBURSEABLE BASIS, TO HELP THEM IN THE IMPORTANT TASK OF COMPLETING THE GEOLOGICAL MAPPING OF MALAYSIA. END COMMENT.
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